Intelligent Trading Technology | White paper

Quantity vs. Quality: An Evolving Research Paradigm

commissioned by visible alpha

INTRODUCTION

Is there a disconnect between the way the sell side and the buy side understand what value looks like when it comes to research?

It seems there is. A survey by Visible Alpha[1] showed that investment management firms are putting more of a focus on how they manage their research provider relationships, which includes how they consume, track, value and pay for research received from those providers. According to the survey, 40 percent of buy-side firms believe that the greatest benefit of MiFID II has been that they can more easily discern the relative quality of research. Investment managers continue to rely on comprehensive usage and consumption data from providers, but they are looking for new ways of consuming and evaluating the research they receive. It's no longer simply about the quantity of content consumed, but about the quality of that research, model or corporate access event.

1 https://info.visiblealpha.com/mifid-ii-survey-results

HOW DID WE GET HERE?

The Markets in Financial Instruments Directive II (MiFID II) rolled out in January 2018 and has forced investment managers all over the globe to take a closer look at their research provider relationships. To improve protection for investors, the new regulations require investment managers to unbundle and pay for research separately from execution commissions. While the full effects of MiFID II are still to be determined, it has been reported that some buy-side firms have already reduced the number of research provider relationships. Therefore, buy-side participants are increasingly implementing a qualitative approach to evaluating research to ensure they are receiving the greatest value from those relationships.

To better understand the reasons for implementing a qualitative approach when it comes to evaluating research, consider one consumer-focused phenomenon. Recently there has been increased mainstream press coverage on how social media companies have allegedly purposefully created 'addictive' platforms. An article from BBC quotes former Mozilla and Jawbone employee Aza Raskin, who designed the "infinite scroll," saying that social media companies aim to make their platforms "'maximally addicting.'"[2] These companies have focused their development on getting users to log in more, to use the service more, to simply stare at it for longer. Why might a social media company create an addictive platform, when it's not in the user's best interest? Raskin explains that big social media companies were aiming to increase the amount of time users spend on their apps for the financial benefits: to secure additional funding, increase stock prices, appeal to new advertisers.

Unfortunately, in this scenario users find themselves spending more and more time using the service while having a less fulfilling experience overall.

In fact, there have been recent reports indicating that Facebook is developing features to allow users to view usage and set limits,[3] and in June 2018, Apple released iOS 12 with new tools to help users better understand and manage screen time and app usage.

Why the sudden shift? Perhaps because social media and technology companies realized they were paying attention to the wrong metrics. They were measuring daily active users, frequency of logins and the amount of time each user spent on the service. These metrics measured quantity, but they lacked in measuring quality. Is a lifetime user one who spends more time on an app but doesn't enjoy

2 https://www.bbc.com/news/technology-44640959
3 https://techcrunch.com/2018/06/22/your-time-on-facebook/

the experience? Or one who spends less time using the product but receives real perceived value and enjoyment?

This scenario parallels that of the evolving investment research paradigm. Spending more time reading research reports, manipulating analyst models or engaging in corporate access doesn’t necessarily equal alpha. However, reading the right research, gaining new and unique insights from financial models and talking to the right analysts at the right time is extremely valuable and can generate high-performing investment ideas.

While research providers want to maximize consumption to increase trading commissions, the buy side is looking to change consumption. Asset managers want to surface the information that is most relevant and important to them, but reduce the amount of incoming and consumed research that doesn’t contribute to investment ideas.

THE IMPACT ON INVESTMENT MANAGERS

With only 24 hours in a day, portfolio managers and analysts have multiple screens, phone calls, research providers and events fighting for their attention and limited time. In fact, with the number of information sources beyond the sell side constantly growing, such as alternative data and independent research providers, time is even more precious and hard to come by. It's not surprising that many investment managers feel overwhelmed by the sheer amount of content they receive via email, websites and platforms, particularly those that were designed to satisfy certain quantitative, rather than qualitative, criteria. Because of this, investment managers struggle to identify which research providers are offering consistently insightful content.

Interestingly, while MiFID II requires unbundling, asset managers have found one of the greatest benefits of the new regulation has been getting a better understanding of research provider quality. The transparency MiFID II requires ensures asset managers are paying for the most impactful research to their investment process.

As a result, the buy side is focusing on quality in a way it simply has not in the past. Investment managers need to be able to justify this spend on research to their clients, so they are beginning to more closely scrutinize the content they receive from various research providers.

Because of this change, investment managers are beginning to realize that a good research provider offers valuable insights that are quickly and easily absorbed – not one who seeks to monopolize their time. The buy side wants to ensure it is paying for high quality, impactful interactions, especially when payment is coming out of their own P&L or is charged to their clients.

Additionally, it's not just about the cost of research or the efficiency of the consumption. Investment managers are interested in the way that research helps them make better and more informed investment decisions, which translates into generating alpha.

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THE SOLUTION

Investment managers are looking for ways to get the most value from what they consume, whether it be research reports, sell-side models, analyst phone calls or other corporate access events. They need information delivered in a way that enables them to deepen their understanding, develop their creativity and generate the kinds of insights that help enhance investment return.

Because of MiFID II's unbundling of research requirements, the buy side now needs to be able to understand which sell-side research houses are providing the most value, and the focus of this judgement is on the quality of the insights and information provided. For the buy side, quantity considerations, such as the amount of research consumed or the time spent reviewing the research, is of secondary importance and could potentially count against a research provider.

There are three areas in which investment managers can increase quality without consuming more content:

1. Discover solutions that surface the most relevant content on the companies that matter
2. Track and rate content consumption to understand what is actually being consumed
3. Implement a formal provider evaluation system, such as a broker vote, to better understand the value of research provider relationships

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INTRODUCING VISIBLE ALPHA

Visible Alpha is redefining the research experience for investment managers and is helping investors receive greater value from the content they consume. With Visible Alpha's solutions, investment managers can see the market more clearly and reduce the amount of manual labor to do so. For example, with Visible Alpha Insights – which captures the forecasts, assumptions and logic from full working models and integrates them into comparable views across analysts – investment teams can get real time access to model updates and instantly see revisions history, surprise analyses and more. By increasing efficiency, analysts can spend more time crafting their ideas and initiating on them.

Visible Alpha's Resource Tracking and Provider Evaluation solutions help asset managers track consumed content, rate that content and evaluate research providers with both quantitative and qualitative measures.

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ABOUT VISIBLE ALPHA

With our solutions, investment managers are able to:

- Completely change the way they engage with research – from how they consume it to how they evaluate it
- Transform their approach to research, driving more value for their firms through enhanced investment decision-making
- Comply quickly and easily with regulations such as MiFID II's research unbundling requirements

Above and beyond this, Visible Alpha supports the development and growth of investment professionals through tools and support at every stage of the investment research workflow.

Visible Alpha Insights
Visible Alpha Insights captures the forecasts, assumptions and logic from full working sell-side models and integrates them into comparable views across analysts. In provides investment managers with deep forecast data on the companies most important to them. With unique analytics and an average of 200 line items per company, this level of data cannot be found anywhere else on the Street.

Resource Tracking
Visible Alpha's Resource Tracking helps firms to track and analyze every research resource they consume, including vendor readership. With a flexible approach to setting rate cards and calculators, investment professionals can value interactions in the most relevant and meaningful way.

Provider Evaluation
Visible Alpha's Provider Evaluation comes with a comprehensive framework that includes a quantitative review of the consumption data and a qualitative feedback process.

Visible Alpha has a wide range of solutions to help empower buy-side firms to consume and use sell-side research more intelligently – supporting both enhanced portfolio returns and the firm's overall investment and compliance cultures.

For more information, visit **visiblealpha.com** or
contact us at **info@visiblealpha.com** or **+1 646 374 4702**.

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A-Team Group provides news and analysis, white papers, webinars, events and more through our two online communities:

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